



**Director of
Central
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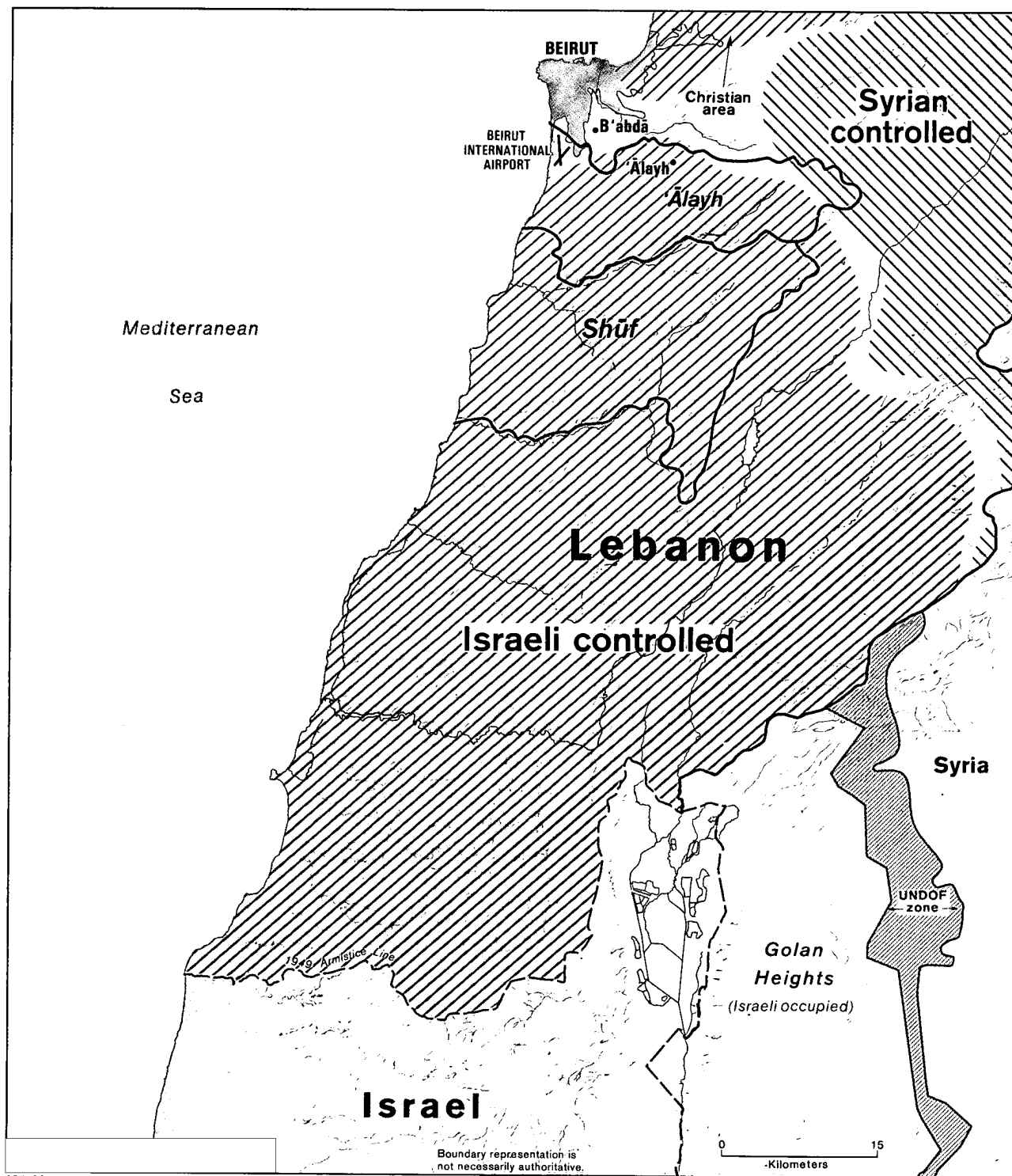
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ISRAEL-LEBANON: Partial Pullback Considered

Support is growing in Israel for a partial pullback of forces in Lebanon. [redacted]

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Many Israelis believe that a withdrawal to more defensible lines—and particularly out of the Shuf region, where Israeli forces have become entangled in Druze-Maronite clashes—could reduce the growing number of casualties. Over the weekend the cabinet discussed a withdrawal and agreed to convene a meeting this week of the Ministerial Defense Committee to discuss various plans for a pullback. According to the US Embassy in Tel Aviv, Israeli and Lebanese military officers met yesterday to review potential withdrawal options. [redacted]

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The Lebanese Army reportedly has done preliminary planning for a deployment into the Shuf and Alayh Districts and has earmarked two brigades currently stationed in Beirut for this purpose. The Israelis believe, however, that the Army can only take over the B'abda-Alayh area. The hills surrounding these towns are the scene of continuing Druze-Maronite fighting. [redacted]

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Comment: Tel Aviv is mindful of US concerns that a unilateral Israeli pullback could lead to partition, and it would consult closely with Washington before proceeding. The Israelis also are apprehensive that Lebanese foes of the withdrawal accord might use such a move to argue that Israel has abrogated it. They will want to wait until the agreement is approved by the Lebanese parliament, which is scheduled to vote on it this week. [redacted]

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Unless the Lebanese Government reaches an agreement with Druze and Christian militia leaders, the Lebanese Army will be unable to move peacefully into the areas vacated by the Israelis. The Druze fear that the Army will assist the efforts by the Phalange-dominated Lebanese Forces militia to seize and subjugate Druze villages. [redacted]

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Lebanese Army Commander Tannous reportedly is trying to work out such an agreement. Without it, the Lebanese Army is unlikely to risk involvement in factional strife that could cause the Army to split again along confessional lines. [redacted]

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EL SALVADOR: Major Pacification Effort

The government has begun an ambitious program of military, economic, and political initiatives aimed at securing San Vicente and Usulután Departments from the guerrillas. [REDACTED]

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[REDACTED] Government civil defense, agricultural, community development, and public works officials are to move in as each area is secured and are to provide redevelopment aid. [REDACTED]

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Meanwhile, a guerrilla radiobroadcast announced on Sunday that insurgent forces had inflicted the worst defeat of the war on the elite US-trained Atlacatl Battalion, which has been operating in remote Morazan Department. The unit was said to have suffered 80 killed and wounded. There has been no confirmation of this report from other sources. [REDACTED]

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Comment: The pacification program in San Vicente and Usulután is the largest and most far-reaching operation undertaken by the government thus far in the war. It has been months in planning and preparation, and the government has much at stake materially and psychologically. [REDACTED]

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The guerrillas will be likely to evacuate the departments and strike hard in another area. The attack on the Atlacatl Battalion may be the first in a series of such actions against the immediate-reaction battalions. The insurgents may hope this will shake the Army's confidence and cause it to draw forces away from the operation. [REDACTED]

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INTERNATIONAL: Disarmament Committee Reconvenes

The 40-member Committee on Disarmament begins a 12-week session this week in Geneva, and to respond to growing public concern a number of nations will make strong efforts to show some progress on arms control.

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Comment: The Committee probably will not show enough progress in multilateral arms control to appease Western domestic groups who are criticizing an apparent lack of results at the INF talks. The Allies, except for the UK, would like to state publicly that the US will soon begin negotiating bans on nuclear testing and weapons in outer space. Most will not break with the US on important issues, however, and they will be likely to settle for formation of a working group to discuss outer space arms control and work on negotiating a chemical weapons ban, short of drafting a treaty.

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The nonaligned countries also will push for superpower negotiations on a test ban, but they will be unable to coordinate their position for technical discussions in this and other areas. Many of them will demand new groups to discuss prevention of nuclear war before completing talks on other existing issues.

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For Moscow, arms control "progress" would entail Washington's resumption of bilateral talks on banning chemical weapons and ASAT and talks with the US and the UK on nuclear testing—or the US being blamed for failure to make headway in these areas. The Soviets, whose stalling tactics earlier this year angered many nonaligned states, apparently will not try to impede discussion of subjects on the Committee's agenda.

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BRAZIL: Arms Sales Prospects

Brazilian arms sales probably will approach record levels this year, largely as a result of purchases by Arab states.

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The Brazilians have sold 12 Xavante light attack planes to Argentina, their first military sale to that country since the conflict in the Falkland Islands. Last year Brazil loaned three maritime patrol aircraft to Argentina.

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Comment: Brazilian arms sales are likely to exceed \$2 billion this year, making the weapons industry profitable for the first time. Transactions involving much larger sums reportedly are being negotiated, but the size of the contracts probably will be reduced as a result of the buyers' limited ability to pay, competition from other suppliers, and unsatisfactory delivery times. Brazil's arms agreement with Israel also could cost it some sales, but it probably will yield to Arab pressures to buy missiles from a West European supplier.

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The cost of Brazil's low-performance weapons makes them attractive to Third World nations seeking an alternative to more established arms suppliers. On the other hand, Brazil's limited ability to produce high-technology weapons, to provide follow-on support, and to replace war losses rapidly from existing inventories will prevent it from sustaining sales at this unusually high annual level.

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USSR-WEST GERMANY: Synthetic Fuel Venture

The Soviets, who are stalled in developing technology for producing synthetic fuels, may soon secure West German assistance for a project to convert Siberian brown coal into oil or gas. [REDACTED]

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For several years the Soviets have been seeking cooperation from West German firms to provide technology and whole plants for the transformation of low-grade Siberian lignite coal into diesel oil, gasoline, or other fuels. [REDACTED] the Soviets plan to build a synthetic fuel industry that, when completed, could eventually earn up to \$20 billion a year from an annual production of 100 million tons of fuel. By comparison, the world's largest synfuel industry, in South Africa, annually produces the equivalent of almost 9 million tons of oil. [REDACTED]

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Soviet officials say contracts for developing the industry could total \$16.5 billion by the end of the century. They expect the first requirement is likely to be a liquefaction plant that would demonstrate the industrial feasibility of producing 1 million tons of fuel annually. It would need Western equipment valued at \$1 billion. [REDACTED]

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One Soviet official recently indicated that funding for the project is likely to be allocated in the five-year plan for 1986-90. It is to be one of the largest energy development projects—along with Siberian oil and gas and Astrakhan sour gas—requiring foreign assistance. [REDACTED]

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Comment: A proposal probably will be discussed next month during Chancellor Kohl's visit to Moscow. West Germany is the world leader in synthetic fuel production technology, and Soviet purchases could sustain West German manufacturers of synthetic fuel plants and equipment during the current economic slump. [REDACTED]

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Initial participation by West Germany is likely to be limited, however, by uncertainties about costs and technological considerations. The Soviets probably cannot develop an industry that can produce the equivalent of 100 million tons of oil annually until after the turn of the century. [REDACTED]

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JAMAICA: New Austerity Program

Prime Minister Seaga has failed to obtain a \$150 million loan from Kuwaiti investors, and he will now have to implement a new austerity program in accordance with an agreement negotiated last month with the IMF. The measures include additional cuts in government spending, shifts of virtually all imports to the costly free-market foreign exchange rate, and further restrictions on government credit. Seaga told US Embassy officials on Saturday that the new measures will disrupt his recovery program and "doom" his political fortunes.

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Comment: The stringent program is essential to maintain the support of the IMF, the World Bank, and commercial lenders. The spending cuts will require major changes in the budget, thereby opening Seaga to strong criticism from the opposition. In the short term, moreover, inflation and already high unemployment are likely to rise, and the drive for increased export earnings will falter.

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COSTA RICA: Economic Protests

The government is beginning to meet public resistance to an IMF-mandated austerity program. Widespread protest demonstrations and the prospect of violence have forced the government to rescind a recent increase in utility rates. Although President Monge is blaming Communist organizers, the US Embassy believes that the protests have extensive popular support.

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Comment: Monge had enjoyed substantial backing for his austerity policies, which are aimed at reducing the pressures related to foreign debt rescheduling. The demonstrations mark the first time he has been attacked personally for poor leadership on economic matters. Future protests are likely as the public becomes more opposed to the austerity measures, and the Communist Party may seek to exploit the discontent.

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NORTH KOREA-CHINA: Visit of Kim Chong-il

Kim Chong-il—the son of North Korean President Kim Il-song—has visited China, according to an East European diplomat with good contacts in Beijing. Although the diplomat says Kim may still be touring the country, the Chinese have not confirmed reports about the trip. 

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Comment: The reported visit appears to be part of the decade-long effort by Kim Il-song to groom his son as his successor. The younger Kim has been steadily assuming more responsibility, and inviting him to Beijing would be the latest of several discrete steps the Chinese have taken toward acknowledging his position. The timing of the trip demonstrates that Beijing's talks with Seoul about the hijacking of 5 May have not disrupted China's ties with North Korea.



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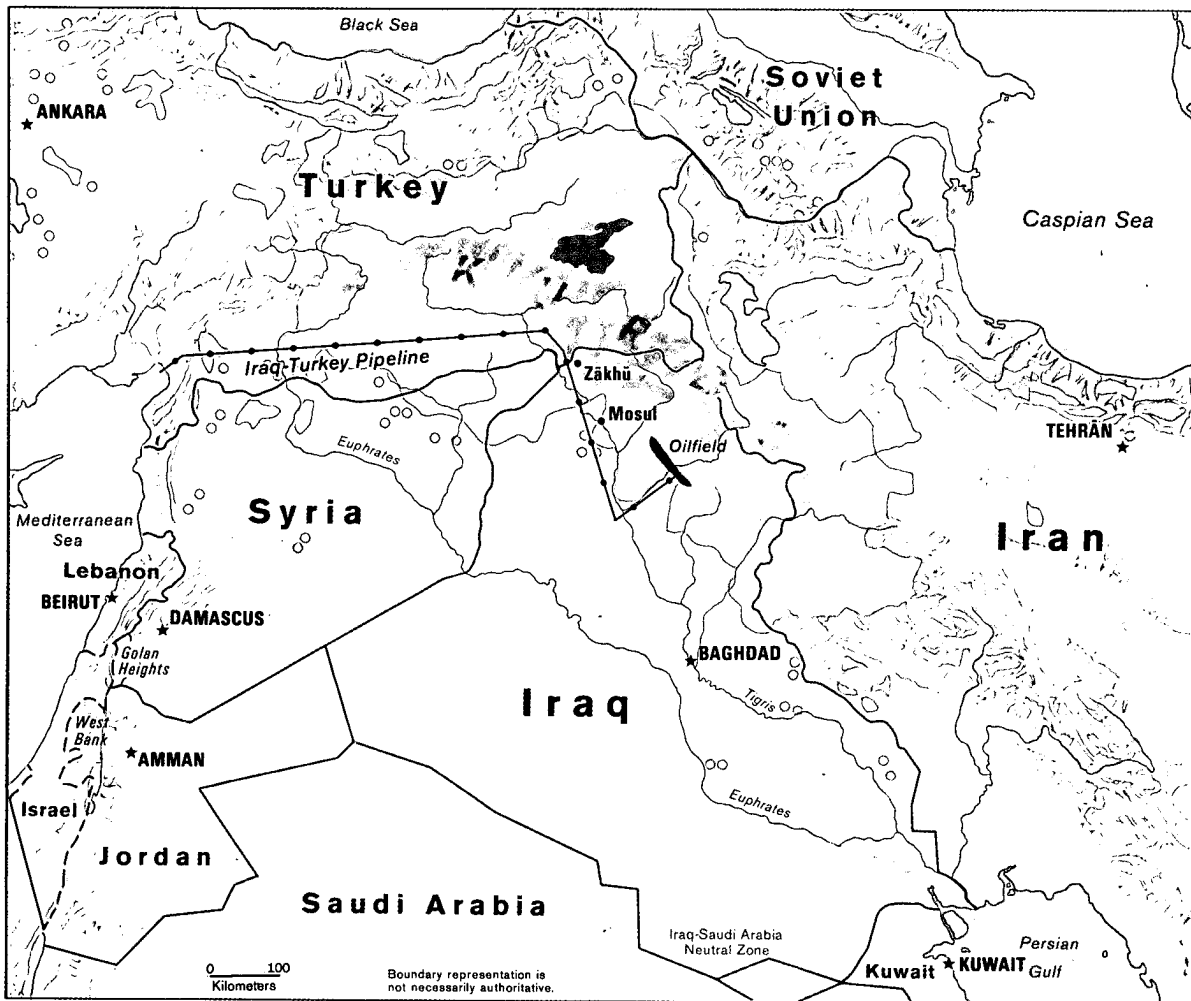
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Special Analysis

TURKEY-IRAQ: Status of Relations

Turkey's recent move against Kurdish dissidents in northern Iraq appears to have been an extension of the military government's efforts to keep domestic terrorism and separatism under control. The Turks pressed the Iraqis hard for permission to carry out the action. They probably hoped that Baghdad's preoccupation with Iran and its dependence on Turkey as a trading partner would overcome any reservations. As long as the war with Iran goes on, the Turks might undertake another operation against the Kurds.

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Both Ankara and Baghdad have long been plagued by Kurdish separatism. Kurds on both sides of the border are demanding an independent Kurdish nation.

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For the Turks, Kurdish irredentism is part of the broader terrorist problem. The military leadership has made great strides against domestic terrorism. Nevertheless, it has been unable to control Kurdish insurgents, who frequently cross Turkey's rugged border with Iraq to escape security dragnets.

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Iraq's concern about the Kurdish problem has grown following recent attacks against government installations and supply convoys in the north.

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The few thousand armed Kurdish dissidents in Iraq can damage the vital oil pipeline that runs north to Turkey and can disrupt traffic on the trade route between Mosul and Zakhu on the Turkish border. Government security forces are primarily concerned with protecting these potential targets rather than responding to isolated guerrilla raids.

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Iraq's preoccupation with the war, which has tied down almost the entire Army, has reduced Baghdad's ability to control the Kurdish forces. This was a major factor in the decision to permit the Turkish operation.

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[redacted]
[redacted] The Treaty of
Friendship of 1946 permits the hot pursuit of criminals in the border
area by security forces of either country. [redacted]

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Economic Ties

The same combination of necessity and grudging cooperation that characterized the interchange between Turkey and Iraq concerning Ankara's anti-Kurd maneuver also undergirds the economic links between the two countries. Turkey hopes to export nearly \$600 million worth of goods to Iraq this year. At the same time, the Turks depend on Iraq for more than 50 percent of their oil. [redacted]

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As a result of war-related trade constraints, Iraq relies heavily on manufactured goods and foodstuffs either produced in or transiting Turkey from Europe. The Iraqis depend on Ankara to ensure that the pipeline—their only oil export route—remains open. The two governments recently signed an agreement to expand the pipeline's capacity from 700,000 barrels per day to about 900,000 barrels per day. [redacted]

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Political Relations

Overall diplomatic relations between Turkey and Iraq are cool. Ankara continues to view Baghdad as a Soviet client and wants to maintain only correct political ties. [redacted]

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The military government is determined to remain neutral in relation to the conflict with Iran. The Turks have been active in the mediation efforts of the Islamic Conference and are pleased by the prestige their position has accorded them in many Middle Eastern capitals. [redacted]

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The Iraqis, while eager to protect their economic relations with Ankara, are suspicious about Turkish motives. This distrust stems largely from a dispute, dating to the collapse of the Ottoman Empire, about the boundary between the two countries. Although these suspicions have been pushed into the background by the war and by the hostility between Iraq and Syria, they are likely to shape Baghdad's view of the Turks for some time to come. [redacted]

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Prospects

Turkey's military leaders hope to leave a stable domestic situation to the civilian politicians who will assume power after the parliamentary elections this fall. Before then, if the Kurds are again seen to be threatening Turkish interests, Ankara might want to launch another operation in Iraq. [redacted]

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If the Iraqis were still tied down by the war, Baghdad probably would acquiesce again. It would see a net benefit in letting the Turks play a dominant role in policing the border. [REDACTED]

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Over the longer term, however, the advent of civilian rule in Turkey is likely to render Ankara less able to act so decisively. The military government has been free of parliamentary constraints, but civilian governments will need to assess the impact of their decisions on public opinion before they act. At the same time, Baghdad's willingness to let the Turks take the lead will decline as it finds itself able to make more troops available to help in reasserting its authority in the northern provinces. [REDACTED]

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Special Analysis

LATIN AMERICA: Collective Action on Debt

The possibilities for joint action by Latin American debtors to obtain better repayment terms on their debts—totaling some \$200 billion—are being more widely discussed. There is no evidence, however, that the leadership of any of the large debtor countries currently is considering forming a "cartel." If IMF-sponsored refinancing programs were to collapse, however, the debtors would be more receptive to joint action rather than making even more painful economic adjustments.

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Bankers are concerned that persistent debt servicing difficulties are increasing the likelihood that some Latin American countries will confront international banks as a bloc.

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Support for Joint Approach

Bankers' concerns will be heightened by a recent call by the Economic Commission for Latin America for regional discussions and a common approach to the debt crisis. An OAS conference, moreover, is scheduled in September to study a joint approach to Latin American financial problems.

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Economic deterioration and election-year rhetoric in Argentina and Venezuela probably will provoke demands by the public in those countries for collective moves. In addition, Ecuador, Nicaragua, Bolivia, and other smaller states will persist in trying to encourage regional approaches.

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High-Level Resistance

Most Latin American political leaders are resisting radical alternatives to current financial programs. De la Madrid has consistently reaffirmed his commitment to repay debts and has opposed calls for collective action.

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Venezuelan President Herrera has said publicly that the OAS debt conference should deal mainly with international financial reform, not

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proposals for radical action. A Chilean spokesman indicates that the Pinochet regime will not join a cartel, [REDACTED]

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These leaders are mainly motivated by national economic self-interest. Large banks are continuing to cooperate with the debtors in their rescheduling programs, and the active involvement of the IMF is tempering frictions between debtors and creditors. The larger states still have a better chance of lining up refinancing on their own than as part of a diverse Latin American group. [REDACTED]

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Prospects

With the exception of Ecuador, Nicaragua, and Bolivia, the Latin American countries are not calling for a moratorium on payments or a repudiation of debts. Most countries, however, appear willing to explore the possibility of regional cooperation—partly in the hope that these discussions alone may prompt bankers to be more forthcoming—but they are not seriously pursuing bloc action. [REDACTED]

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Joint action will not succeed without the participation of at least one of the major debtors—Brazil, Mexico, Argentina, or Venezuela. Regional discussions of possible collective action would facilitate the formation of a negotiation bloc, however, if key debtors do not see any chance of resolving their financial troubles through existing arrangements with commercial banks and the IMF. [REDACTED]

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The main threat to the current arrangements comes from the reluctance of smaller US banks and many European and Japanese banks to refinance loans or to increase the amount of credit they extend in Latin America. If the major banks are unable to get remaining creditors to cooperate, or if they cannot cover the resulting shortage of funds, one or more of the current refinancing plans could become unworkable. [REDACTED]

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Similarly, political resistance to IMF-related austerity is mounting. If any country substantially relaxes spending constraints to reduce unrest, it could significantly slow IMF disbursements and commercial lending. [REDACTED]

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With receipts and credit slowed, the rescue programs also might be disrupted. The first collapse could set off others, ultimately provoking one of the large debtors to make radical changes in the terms of debt service in its favor. Other debtors would quickly coalesce around the new leader. [REDACTED]

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